Chapter Three

The Revenue Outlook

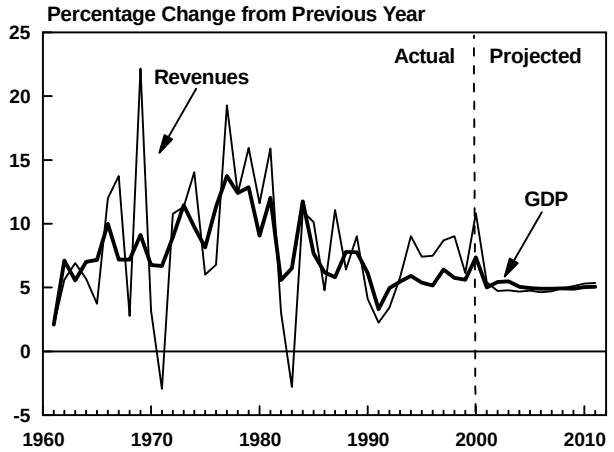
The Congressional Budget Office estimates that total federal revenues will exceed $2.1 trillion in fiscal year 2001 if current policies remain unchanged, marking the ninth consecutive year in which the growth of revenues has outstripped the growth of the nation's gross domestic product (see Figure 3-1). Revenues are expected to grow more slowly than GDP (nominal) through 2007 and then faster than GDP through 2011. In that year, revenues are projected to be $3.4 trillion, or about 20.4 percent of GDP.

CBO expects that the growth of receipts will be slower than the rapid pace of the past few years. From 1994 to 2000, revenues rose at an average annual rate of 8.3 percent, much faster than GDP. In 2000, at 10.8 percent, the growth of receipts was faster than in any year since 1987 (when growth was subject to a one-time boost from the Tax Reform Act of 1986). Consequently, as a share of GDP, revenues rose from 18.1 percent in 1994 to a post-World War II high of 20.6 percent in 2000—a level exceeded only once, in 1944 (see Figure 3-2).

Although slowing in 2001, the growth of receipts, projected at 5.4 percent over the previous year, still outpaces the projected growth of GDP, pushing the ratio of receipts to GDP to 20.7 percent in 2001, which is expected to become the new post-war peak. In 2002, the growth of receipts is projected to slow further, to 4.7 percent—less than the growth of GDP—so as a percentage of GDP, receipts will slip to 20.5 percent. The growth of receipts remains at about that rate through 2007 but as a percentage of GDP continues to fall, to 20.2 percent. After 2007, the growth of receipts is expected to rise, to 5.4 percent in 2011, and to increase relative to GDP, reaching 20.4 percent by the end of the projection period.

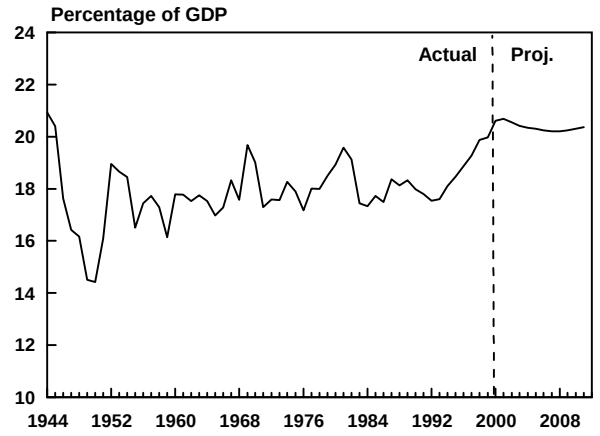
The current revenue outlook is $919 billion higher through 2010 than CBO projected last July (see Table 3-1). About seven-eighths of that increase—or about $800 billion—stems from changes in CBO's economic forecast, which causes a boost in receipts from individual and corporate income and social insurance taxes. The net effect of recently enacted legislation—primarily the Community Renewal

Figure 3-1.
Annual Growth of Federal Revenues and GDP, Fiscal Years 1960-2011



SOURCE: Congressional Budget Office.

Figure 3-2.
Total Revenues as a Share of GDP, Fiscal Years 1944-2011



SOURCE: Congressional Budget Office.

Tax Relief Act of 2000 (H.R. 5662) and the FSC (Foreign Sales Corporation) Repeal and Extraterritorial Income Exclusion Act of 2000 (H.R. 4986)—reduces projected revenues by about $37 billion over the 10 years from 2001 to 2010. The remainder of the increase since July results from a number of adjustments in the methodology and assumptions that determine how much tax is generated by the tax base. Those technical revisions total $153 billion over the 10 years.

Federal revenues consist of individual income taxes, corporate income taxes, social insurance taxes, excise taxes, estate and gift taxes, customs duties, and miscellaneous receipts. Individual income taxes produce about half of total revenues, an amount equal to roughly 10 percent of GDP (see Table 3-2 and Figure 3-3). Corporate income taxes contribute about a tenth of revenues, equaling approximately 2 percent of GDP. Social insurance taxes (including Social Security taxes, which are off-budget) are the second largest source of revenues, equaling about a third of total receipts and less than 7 percent of GDP. Other taxes and miscellaneous receipts, including profits from the Federal Reserve System, make up the balance.

- *Individual income tax receipts*, bolstered primarily by higher realizations of capital gains and increases in the effective tax rate, have fueled the rapid growth of revenues relative to GDP over the past few years. Because those trends are not expected to continue, the growth of revenues will slow over the next few years. The higher realizations of capital gains stemmed largely from the sharp rise in stock prices. Increases in the effective tax rate were the result of growth in real incomes generally, which increased the amount of income taxed at higher marginal tax rates (the tax rates that apply to an additional dollar of income), and of a rapid rise in income among high-income taxpayers, who are taxed at higher marginal rates.

  Although the growth of individual income tax receipts is projected to slow as capital gains in particular play a smaller role in boosting receipts, higher nominal income raises the average effective tax rate as the number of taxpayers affected by the alternative minimum tax (AMT) increases and growth in real income subjects more income to higher marginal tax rates. For the first half of the projection period of fiscal years 2001 to 2011, the depressing effect of slackening capital gains overwhelms the effect of a rising effective tax rate, lowering individual income tax receipts as a share of GDP. Thereafter, the increase in the effective tax rate is the more important effect, so the share of GDP rises. That pattern tends to drive the ratio of total receipts to GDP, largely dominating the effects of corporate income taxes and excise taxes, which tend to fall relative to GDP over the 11 years.

- *Corporate income taxes* contributed somewhat to the increase in revenues in the 1990s, as profits improved over their performance of the 1970s and 1980s. But from 2001 to 2011, profits are projected to recede from the unusually high levels of the late 1990s. As a result, projected corporate income tax receipts as a percentage of GDP are expected to fall somewhat from 2.1 percent to 1.9 percent.

- *Social insurance taxes*, consisting largely of taxes for the Medicare program and Social Security, have changed little as a share of GDP in the past decade. From 2001 to 2011, they are

also expected to remain essentially stable at about 6.6 percent of GDP.

- *Excise taxes*, although a relatively small revenue source, are expected to reduce receipts as a share of GDP during the projection period, dropping from 0.7 percent to 0.6 percent of GDP from 2001 to 2011. That share falls because many excise taxes are levied per unit or transaction rather than as a percentage of value. Receipts, therefore, tend to rise mainly with increases in real, rather than nominal, GDP.

- All other revenue sources—estate and gift taxes; customs duties; and miscellaneous receipts, including receipts from the Federal Reserve System—are expected to remain just under 1 percent of GDP throughout the projection period.

Table 3-1.
Changes in CBO's Projections of Revenues Since July 2000 (By fiscal year, in billions of dollars)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Total, 2001-2010
July 2000 Projection of Revenues	2,109	2,202	2,290	2,380	2,486	2,594	2,706	2,826	2,960	3,102	n.a.
Legislative Changes											
Individual Income	-1	-1	-2	-2	-2	-2	-3	-3	-3	-3	-22
Corporate Income	0	-1	-1	-1	-1	-1	-2	-2	-2	-2	-14
Other	-1	-1	0	0	0	0	0	0	0	0	-1
Subtotal	-2	-2	-3	-3	-3	-4	-4	-5	-6	-5	-37
Economic Changes											
Individual Income	-4	-1	10	22	31	41	51	61	72	84	366
Corporate Income	4	15	24	29	31	33	36	42	49	58	319
Social Insurance	-3	-2	2	8	12	16	20	26	30	33	143
Other	-4	-5	-4	-3	-2	-2	-1	-1	-2	-2	-26
Subtotal	-6	7	32	56	72	88	106	128	148	173	802
Technical Changes											
Individual Income	25	20	12	8	5	2	0	-2	-4	-6	60
Corporate Income	11	11	10	10	10	9	8	8	7	6	90
Other	-3	-1	1	1	1	0	1	2	1	2	4
Subtotal	33	29	24	20	15	11	9	7	4	2	153
Total Changes											
All Sources	25	34	53	73	84	95	110	129	146	170	919
January 2001 Projection of Revenues	2,135	2,236	2,343	2,453	2,570	2,689	2,816	2,955	3,107	3,271	n.a.

SOURCE: Congressional Budget Office.

NOTE: n.a. = not applicable.

Table 3-2.
CBO's Projections of Revenues (By fiscal year)

	Actual 2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
						In Billions of Dollars						
Individual Income	1,004	1,076	1,125	1,176	1,230	1,289	1,354	1,424	1,500	1,583	1,675	1,774
Corporate Income	207	215	217	226	236	246	255	264	276	289	303	319
Social Insurance	653	686	725	762	797	840	879	921	963	1,010	1,059	1,110
Excise	69	71	74	76	78	81	83	86	88	91	94	97
Estate and Gift	29	30	32	34	35	36	37	39	43	46	48	52
Customs Duties	20	21	23	24	25	26	27	27	28	29	30	31
Miscellaneous	43	36	41	44	51	52	54	55	57	59	61	63
Total	2,025	2,135	2,236	2,343	2,453	2,570	2,689	2,816	2,955	3,107	3,271	3,447
On-budget	1,545	1,630	1,703	1,782	1,864	1,950	2,040	2,136	2,243	2,360	2,489	2,628
Off-budget[a]	481	504	532	561	589	620	649	680	712	746	782	819
						As a Percentage of GDP						
Individual Income	10.2	10.4	10.3	10.2	10.2	10.2	10.2	10.2	10.3	10.3	10.4	10.5
Corporate Income	2.1	2.1	2.0	2.0	2.0	1.9	1.9	1.9	1.9	1.9	1.9	1.9
Social Insurance	6.6	6.6	6.7	6.6	6.6	6.6	6.6	6.6	6.6	6.6	6.6	6.6
Excise	0.7	0.7	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Estate and Gift	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Customs Duties	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Miscellaneous	0.4	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Total	20.6	20.7	20.5	20.4	20.3	20.3	20.2	20.2	20.2	20.3	20.3	20.4
On-budget	15.7	15.8	15.7	15.5	15.5	15.4	15.4	15.3	15.3	15.4	15.5	15.5
Off-budget[a]	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.8

SOURCE: Congressional Budget Office.

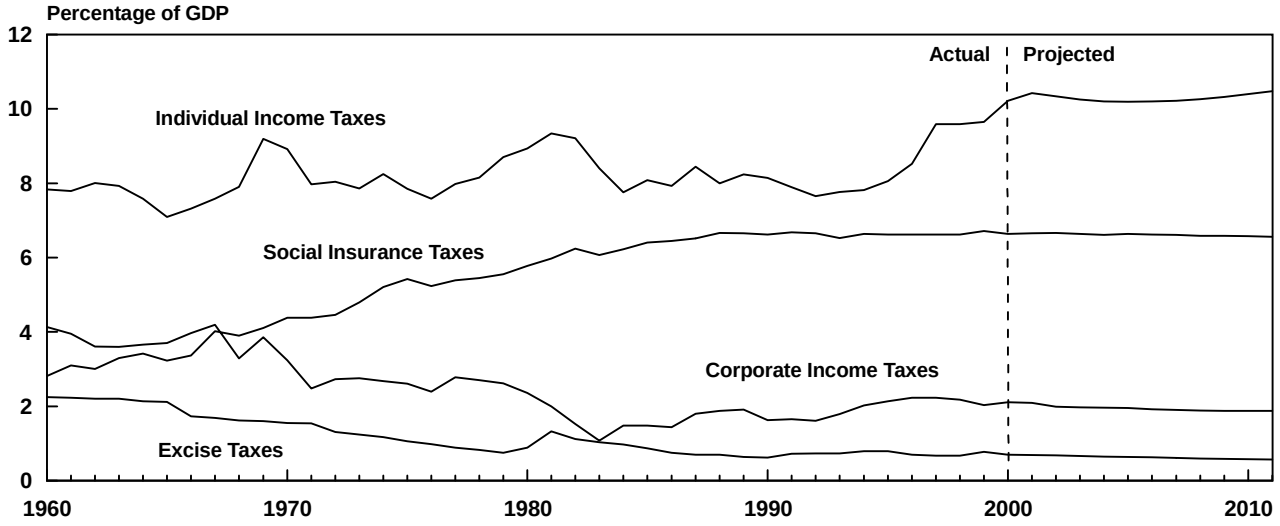
a. Social Security.

Individual Income Taxes

Individual income taxes account for most of the recent rise in revenues as a percentage of GDP. From 1993 to 1998, those receipts averaged growth of more than 10 percent a year. In fiscal year 1999, partly because of the tax cuts enacted in the Taxpayer Relief Act of 1997, they slowed to their lowest rate of increase since 1992. But in fiscal year 2000, they jumped more than 14 percent, reaching their highest share of GDP ever. Their share is expected to peak in 2001 and then to slowly recede as some of the factors that caused the rise moderate. But in 2006, the factors tending to boost the share of individual tax receipts begin to dominate, so by 2011, those receipts as a percentage of GDP reach a new historical peak.

Individual income tax projections over the 2001-2010 period are about $400 billion higher than in July. More than $350 billion of that change is due to the revised economic forecast. About $60 billion of the increase is from technical changes, most importantly revisions in the capital gains projection, adjustments for unexplained higher-than-expected tax collections since July, and some minor changes in

Figure 3-3.
Revenues, by Source, as a Share of GDP for Fiscal Years 1960-2011



SOURCE: Congressional Budget Office.

CBO's methodology. Legislation reduced the projections by about $20 billion.

Sources of Recent Growth in Individual Income Taxes

Historically, individual income taxes have tended to grow only slightly faster than GDP, with few exceptions. In 1969, for example, a surtax caused income tax receipts to increase significantly faster than GDP; and before the tax code was indexed, inflation pushed the growth of income tax receipts well above that of the economy by effectively decreasing the levels of real income at which higher tax rates applied. But those phenomena were largely temporary and were followed by years in which the growth of income tax receipts fell below that of GDP. From 1994 to 2000, however, the annual growth of those receipts surpassed that of the economy for reasons unrelated to new tax legislation. In fact, in 1998 and 1999, receipts increased as a percentage of GDP despite new tax breaks concerning children and education.

CBO examined a sample of detailed tax-return data to identify the sources of the recent growth in individual income tax liabilities as a percentage of GDP. Liabilities (what taxpayers determine they owe to the government) roughly translate into receipts (what the government receives). An analysis of tax years (the years in which the tax liabilities are incurred) 1994 through 1998 attributes the surge to four sources. (As described below, Table 3-3 traces the share of the growth attributable to each of the four sources.)[1]

The first significant source of the increase in individual income tax liabilities as a percentage of GDP was the rapid growth of components of GDP that are taxable to individuals. (For more information on the relationship between tax liability, taxable income, and GDP, see Box 3-1.) Taxable personal income—the sum of wages, interest, dividends, proprietors' income, and rental income, as measured in the national income and product accounts (NIPAs)—grew faster than GDP from 1994 to 1998. The resulting rise in the proportion of taxable personal income in GDP raised the tax base for individual income taxes and accounted for roughly 20 percent of the growth of tax liabilities in excess of the growth of GDP over that period.

1. For consistency, the percentage contribution of each of the four sources is calculated using the amount of tax liability that would have accrued if the child and education tax credits that became effective in tax year 1998 had not been enacted.

The next two sources are components of adjusted gross income (AGI)—the actual income base of the individual income tax—which rose more rapidly than taxable personal income. Capital gains realizations, which are not included in either GDP or taxable personal income, account for a large part of the growth in AGI. Between 1994 and 1998, realizations of capital gains nearly tripled, with most of that increase occurring before the cut in tax rates for them in 1997. Taxes on capital gains accounted for roughly 30 percent of the growth of those liabilities relative to the growth of GDP from 1994 to 1998.

Other components of AGI that are not part of taxable personal income or GDP also rose more rapidly than both of those measures—especially retirement income from distributions from 401(k) plans and individual retirement accounts and from taxable Social Security benefits. The growth of the retirement and nonretirement components together accounted for about 6 percent of the increase in liabilities relative to the growth of GDP from 1994 to 1998.

The most significant source of the growth of income taxes relative to GDP was the increase in the effective tax rate. In tax years 1995 to 1998, increases in the effective rate (on income other than capital gains) accounted for more than 40 percent of the growth of liabilities in excess of the growth of GDP. Increases in real income for taxpayers generally placed more income into higher tax brackets. That phenomenon alone accounted for more than half of the increase in income tax liabilities relative to GDP that resulted from the rise in the effective tax rate. The remainder was due to income growth concentrated at the top of the income distribution, which raised the effective tax rate by increasing the proportion of income taxed at the highest rates. Even though no income group was subjected to higher statutory tax rates, a larger share of income accrued to taxpayers with the highest tax rates. (See Figure 3-4.)

Although the proximate causes of the surge in individual income tax receipts can be identified by examining tax filings, the underlying causes are more

Table 3-3.
Shares of Growth of Individual Income Tax Liabilities in Excess of Growth of GDP, by Source, Tax Years 1995-1998 (In percent)

Source of Growth of Tax Liabilities	1995	1996	1997	1998[a]	Total, 1995-1998[a]
Taxable Personal Income (TPI) Grew Faster Than GDP	21	12	14	33	20
Adjusted Gross Income (AGI) Grew Faster than TPI					
Capital gains taxes grew faster than TPI	21	52	30	15	30
Other AGI grew faster than TPI	14	4	9	2	6
Changes in the Effective Rate on AGI					
Effect of real growth on rate	21	17	27	29	24
Growth in incomes of high-income taxpayers	23	15	20	21	20
Total	100	100	100	100	100
Memorandum:					
Growth of Individual Income Tax Liabilities in Excess of Growth of GDP (Billions of dollars)	27	39	35	40	141

SOURCE: Congressional Budget Office using data from the Internal Revenue Service's *Statistics of Income, 1994-1998*.

a. The estimates of 1998 tax liabilities do not include the child and education credits enacted in the Taxpayer Relief Act of 1997.

Box 3-1.
Tax Bases and Tax Liability

The ratio of tax receipts to gross domestic product (GDP) varies for reasons other than changes in tax law. In particular, the bases on which taxes are imposed differ from GDP, and their growth is sometimes faster or slower than that of GDP. Although the bases for taxes on individual and corporate income and social insurance are similar to gross domestic product, they differ from GDP in a number of important respects.

Individual Income Tax Base

Taxable personal income is the first approximation of the individual income tax base. It comprises dividends, interest, wages and salaries, rent, and proprietors' income. It does not include depreciation, indirect business taxes, fringe benefits, or retained corporate profits.

Not all of that income is taxed, however. Some accrues to tax-exempt entities such as hospitals, schools, cultural institutions, and foundations; some is earned in a form that is tax-exempt, such as income from state and local bonds; and some is tax-deferred, such as income from retirement accounts. Also, personal interest and rental income contain large components of imputed income—income that is not earned in a cash transaction, including personal earnings within pension funds and life insurance policies and from owner-occupied housing—which is not taxable. Consequently, a large amount of interest, dividend, and rental income is excluded from the taxable base of the income tax.

Taxpayers make further adjustments, both additions and subtractions, to taxable personal income to derive *adjusted gross income* (AGI). *Capital gains realizations*—the increase in the value of assets between the time they are purchased and sold—are added to taxable personal income. Contributions from income to tax-deductible individual retirement accounts and 401(k) programs are excluded, but distributions to retirees from those programs are included. Taxpayers also make a variety of other, smaller adjustments.

Exemptions and *deductions* are subtracted from AGI to yield taxable income, which is then subject to progressive tax rates (that is, rates that rise as income rises). The resulting tax may then be subject to further adjustments in the form of *credits*, such as the child tax credit for taxpayers with children under 17, which reduce the taxpayers' *tax liability*. An important factor in calculating individual tax liability is the *alternative minimum tax* (AMT), which requires some taxpayers to calculate their taxes under a more limited set of exemptions, deductions, and credits. Taxpayers then pay the higher of the AMT or the ordinary tax. The ratio of tax liability to AGI is called the *effective tax rate on AGI*.

Corporate Income Tax Base

Corporate income in GDP is calculated on the basis of *economic depreciation*—the dollar value of productive capital assets that have been used up. For tax purposes, however, corporations calculate *book profits*. Those profits are calculated on the basis of *book*, or *tax, depreciation*, which is typically more generous than economic depreciation; that is, the capital is assumed to be used up faster than it actually is, allowing firms a greater reduction in their reported (and therefore taxable) profits.

The measure of book profits must then be adjusted to remove profits of the Federal Reserve System, which are counted with corporate profits in the national accounts but as federal revenues, as miscellaneous receipts, in the budget. They are also adjusted to allow for the taxation of U.S. income earned by foreign corporations and the deferral of most foreign income earned by U.S. corporations. Those and other, smaller adjustments yield *taxable income* for corporations. If taxable income is negative (that is, the firm loses money), the loss (within limits) may be carried back or forward to be netted against previous or future taxable income to lower taxes in those other years. A tax rate is applied to determine tax liability, which credits may reduce further. The ratio of corporate taxes to taxable income is the *average tax rate*.

Social Insurance Tax Base

Social insurance taxes, the other big source of receipts, use payroll as their base. Those taxes largely fund Social Security and Hospital Insurance (Part A of Medicare). Social Security taxes are imposed as a percentage of pay up to a *taxable maximum* that is indexed for wage growth in the economy. Medicare's Hospital Insurance taxes are not subject to a taxable maximum.

Despite the many adjustments that must be made to calculate the true tax bases, a ready approximation is the sum of wages and salaries and corporate book profits (see Chapter 2). Those items pick up much of the bases of the individual income, corporate income, and social insurance taxes and therefore constitute the bulk of taxed income.

difficult to discern. In particular, it is difficult to isolate the role of the extraordinary rise in the stock market. The potential role of the stock market in boosting individual income taxes, and in generating receipts from other tax sources, is discussed in more detail below.

Revenues in 2000

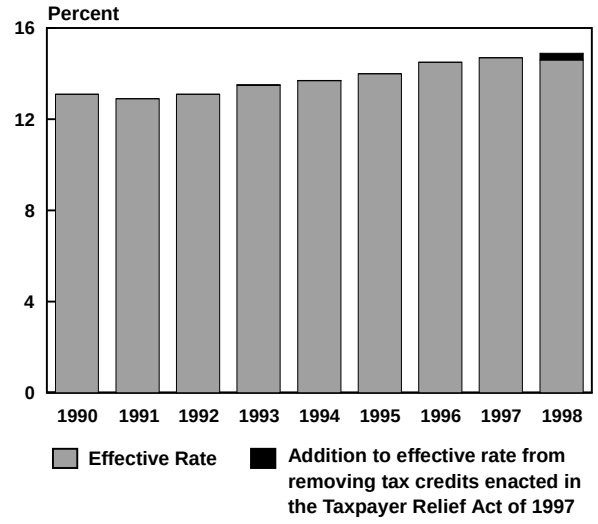
After three years in which revenues exceeded one-year-ahead projections by substantial amounts, CBO's January 1999 revenue projection was largely on target. But in fiscal year 2000, revenues again exceeded CBO's projection by a substantial amount. In January 2000, CBO estimated that 2000 revenues would total $1,945 billion. However, the end-of-year figure was $2,025 billion, or $80 billion more. Individual income taxes accounted for three-quarters of the difference (see Table 3-4). About half of the $60 billion underestimate of individual income taxes stemmed from higher-than-expected withholding. The other half was from nonwithheld receipts, largely due to the return of the "April surprise" of unexpected final payments in the spring of 2000.

Table 3-4.
Actual Revenues in Fiscal Year 2000, by Source, Compared with CBO's January 2000 Projections (In billions of dollars)

Source	Actual 2000 Revenues	CBO's January 2000 Projections	Difference
Individual Income Taxes			
Withheld	780	749	31
Nonwithheld	358	331	27
Refunds	-134	-135	1
Subtotal	1,004	945	60
Corporate Income Taxes	207	189	18
Social Insurance Taxes	653	653	0
Excise Taxes	69	68	1
Other Revenue Sources	92	90	2
Total	2,025	1,945	80

SOURCE: Congressional Budget Office.

Figure 3-4.
Effective Tax Rate on Individual Income, Tax Years 1990-1998



SOURCE: Congressional Budget Office.

Fiscal year 2000 individual income tax receipts jumped 14 percent over their level in fiscal year 1999—not only a substantial increase over the 6.1 percent of the previous year, but more than in any year in the 1990s. As a result, individual income tax receipts exceeded $1 trillion for the first time and reached a new peak as a percentage of GDP, exceeding 10 percent for the first time (see Table 3-5).

Capital gains realizations are notoriously difficult to predict. They constitute a relatively small percentage of tax receipts, however, which mutes their role in generating large errors in revenue projections (see Table 3-6). The January 2000 estimate of realizations in tax year 1999, which are important for fiscal year 2000 receipts because much of the resulting tax is paid with the subsequent filing of tax returns, was $500 billion, compared with actual realizations of about $555 billion.

Expected Pattern of Future Receipts

The growth of individual income tax receipts is expected to slow substantially in 2001, to 7.1 percent. That increase still exceeds the growth of GDP, so in 2001 individual income tax receipts as a percentage of GDP are projected to reach a new peak, 10.4 percent (see Table 3-5). Growth is then expected to slow further to 4.6 percent for three years and then increase each year through the end of the projection period, approaching 6 percent in 2011. So in that year, receipts as a share of GDP are projected to surpass previous highs, reaching 10.5 percent.

A cooling of the economy is partly responsible for the slower growth at the beginning of the projection period: according to CBO's economic forecast, the growth of GDP is expected to slow from 7.3 percent in 2000 to an average of 5.2 percent over the next four years. But other, tax-specific factors also affect the path of individual tax receipts, namely, the four factors described above that explain the rapid growth of receipts during the 1995-1998 period: taxable personal income relative to GDP, capital gains realizations, taxable retirement income and other components of AGI that are not taxable personal income, and the effective tax rate.

In CBO's 2001-2011 economic projections, taxable personal income decreases as a share of GDP, which tends to slow the growth of receipts and further reduce their share of GDP over time. Much of that decrease in income, however, is in the more lightly taxed interest and dividend components of income rather than in wages and salaries. Consequently, the decline of taxable personal income as a share of GDP only slightly lowers the ratio of total receipts to GDP over the period of 2001 to 2011.

The components of AGI fare differently in the projections. Capital gains realizations gradually resume their historical relation to GDP (with due allowance given to the effect of lower capital gains tax rates on taxpayers' willingness to realize gains), slowing the growth of receipts and reducing their share of GDP. As a result, receipts are about $120 billion lower in 2011 than they would have been if they maintained the same share of GDP as in 2000.

Table 3-5.
CBO's Projections of Individual Tax Receipts and the Tax Base (By fiscal year)

	Actual 2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Individual Income Tax Receipts												
In billions of dollars	1,004	1,076	1,125	1,176	1,230	1,289	1,354	1,424	1,500	1,583	1,675	1,774
As a percentage of GDP	10.2	10.4	10.3	10.2	10.2	10.2	10.2	10.2	10.3	10.3	10.4	10.5
Annual growth rate	14.2	7.1	4.6	4.6	4.6	4.8	5.0	5.2	5.3	5.5	5.8	5.9
Taxable Personal Income												
In billions of dollars	6,952	7,314	7,684	8,066	8,428	8,800	9,193	9,610	10,036	10,478	10,948	11,440
As a percentage of GDP	70.7	70.9	70.6	70.3	69.9	69.5	69.2	69.0	68.7	68.3	68.0	67.6
Annual growth rate	6.7	5.2	5.1	5.0	4.5	4.4	4.5	4.5	4.4	4.4	4.5	4.5
Individual Receipts as a Percentage of Taxable Personal Income	14.4	14.7	14.6	14.6	14.6	14.7	14.7	14.8	14.9	15.1	15.3	15.5

SOURCE: Congressional Budget Office.

NOTE: The tax base in this table reflects income as measured by the national income and product accounts rather than as reported on tax returns.

Other components of AGI, especially retirement income, become more important, raising the growth of individual income tax receipts slightly and slowly increasing their share of GDP over time. The growth of retirement income adds roughly $30 billion to receipts in 2011 relative to what they would have been with a constant receipts-to-GDP ratio.

The effective tax rate rises as a consequence of higher incomes. Because the alternative minimum tax is not indexed for inflation, higher nominal incomes subject more taxpayers to it. In addition, even though the regular income tax is indexed for inflation, real growth in incomes causes more people to be taxed at higher marginal rates because of the progressive rate structure. Those two factors tend to boost the growth of receipts and cause the receipts-to-GDP ratio to rise over time. The effects of the AMT raise receipts in 2011 by about $30 billion relative to what they would have been if the receipts-to-GDP ratio

Table 3-6.
Actual and Projected Capital Gains (In billions of dollars)

	Realizations		Liabilities		Receipts[a]		Receipts as a Percentage of Total Individual Income Tax Receipts
	Level (CY)	Percentage Change	Level (CY)	Percentage Change	Level (FY)	Percentage Change	
1990	124	-20	28	-21	32	-14	7
1991	112	-10	25	-11	27	-17	6
1992	127	14	29	16	27	1	6
1993	152	20	36	25	32	20	6
1994	153	0	36	0	36	12	7
1995	180	18	44	22	40	10	7
1996	261	45	66	50	54	36	8
1997	365	40	79	19	72	33	10
1998	455	25	89	12	84	16	10
1999	555	22	109	22	98	17	11
2000	652	18	129	19	118	20	12
2001	652	0	129	0	129	9	12
2002	619	-5	121	-6	125	-3	11
2003	593	-4	116	-5	119	-5	10
2004	574	-3	111	-4	114	-4	9
2005	561	-2	108	-3	110	-3	9
2006	553	-1	106	-2	107	-2	8
2007	551	0	106	-1	106	-1	7
2008	554	0	106	0	106	0	7
2009	560	1	107	1	106	1	7
2010	571	2	109	2	108	1	6
2011	586	2	111	2	110	2	6

SOURCES: Congressional Budget Office; Department of the Treasury.

NOTE: CY denotes data on a calendar year basis, and FY denotes data on a fiscal year basis. Realizations represent net positive long-term gains. Data on realizations and liabilities after 1998 and data on receipts for all years are projected by CBO.

a. Receipts approximate the timing of the payments of liabilities during fiscal years.

remained constant. (Those receipts include the additional receipts from disallowing child and education tax credits against the AMT after 2001.) The effects of real growth on the regular income tax raise 2011 receipts by approximately $75 billion relative to what they would have been if the receipts-to-GDP ratio remained constant. Although the rapid income growth among high-income taxpayers is not expected to further increase the effective tax rate beyond 2001, those taxpayers are expected to maintain the shares of income they gained during the recent economic boom. As a result of that distributional change, CBO expects that the growth of receipts will slow and the receipts-to-GDP ratio will level off.

Together, the four tax-specific factors will cause the growth of individual receipts to slow and the receipts-to-GDP ratio to decline at first and then rise again. Initially, the pattern of lower capital gains realizations relative to GDP and slower growth of taxable personal income dominates and causes the receipts-to-GDP ratio to fall. Slowly, however, the other effects—the growth of taxable retirement income and the higher effective tax rate resulting from real income growth—cause the ratio to rise after 2005 so that it achieves a new postwar peak by the final year of the projection.

Clearly, the future course of most of these factors is very uncertain. The implications of different courses for the effective tax rate and economic growth for the budget surplus are discussed in Chapter 5.

Corporate Income Taxes

In recent years, corporate income tax receipts have grown more rapidly than the overall economy. From 1995 to 1998, corporate income tax receipts as a percentage of GDP grew to levels not achieved since 1980. That performance was largely driven by very strong growth in corporate profits. In 1999, corporate income tax receipts as a percentage of GDP slipped as profit growth slowed. But in 2000, receipts as a share of GDP rebounded as profits grew strongly again.

CBO projects that from 2001 to 2011, corporate income tax receipts will no longer grow more rapidly than the economy, and over the next couple of years, they will grow little, if at all (see Table 3-7). Receipts rise very modestly in 2001, mainly because of the lagged effects of the strong profit growth recorded in 2000, and remain about the same in 2002. Corporate receipts begin to grow again in 2003 and continue to grow through 2011. As a percentage of GDP, they fall from 2.1 percent in 2000 and 2001 to 2.0 percent in 2002 through 2004 and 1.9 percent in 2005 and remain at that level thereafter.

The projection of corporate income tax receipts is nearly $400 billion more over the period of 2001 to 2010 than CBO's July projection. More than $300 billion of that increase is due to the change in the economic forecast. About $90 billion of it is due to technical revisions stemming from higher-than-expected corporate tax collections since July.

Projections of corporate income tax receipts are always subject to a great deal of uncertainty, although their relatively small size dampens the effect of that uncertainty on projections of total revenues. Much of the uncertainty stems from the fluctuation of corporate profits. Profits are essentially the residual income in an economy—what remains for the owners of firms after all of the other productive inputs have been compensated. As a result, profits tend to vary much more over time than do other sources of taxable income, making them difficult to project.

Uncertainty also arises from unexpected movements in the average tax rate (total corporate receipts as a percentage of total taxable profits). Those unexpected movements have been greatest following major changes in corporate tax law, such as occurred in 1986.[2] Over much of the period since then, the average tax rate has been relatively stable, so CBO's projection error has typically resulted from profits that grew at rates different from those anticipated.

The slow growth of corporate income tax receipts in CBO's projection is the result of projected slow growth in taxable profits. A factor responsible for part of the slow growth of profits over the next several years is the projected behavior of book depre-

2. See Congressional Budget Office, *The Shortfall in Corporate Tax Receipts Since the Tax Reform Act of 1986*, CBO Paper (May 1992).

ciation (the allowance for depreciation that firms are permitted for tax purposes). Investment in assets with short depreciable lives for tax purposes has risen sharply in recent years and is expected to rise strongly in 2001 and 2002 and then to slow. Thus, in 2001 and 2002, depreciation for tax purposes is expected to grow rapidly, followed by a gradual moderation in its growth. (The behavior of tax depreciation is the biggest reason that CBO's projections of book profits, which are close to the income measure on which taxes are collected, differ from the commonly used corporate economic profits that appear in the NIPAs as part of GDP.)

CBO makes several adjustments to book profits to produce an even better approximation of the corporate tax base, called "taxable corporate profits." First, CBO's measure excludes corporate profits from foreign subsidiaries of U.S. firms. Taxes on those profits are largely deferred under the corporate income tax until the profits are repatriated to the U.S. parent corporation, and even then they typically are not taxed because of a credit for foreign taxes paid on that income. Second, CBO's measure excludes profits of S corporations, which are usually smaller firms that qualify for taxation as partnerships. As such, their profits are considered to flow through automatically to the shareholders and are taxed as individual rather than corporate income. Other adjustments include subtracting corporate income taxes paid to state and local governments and the profits of the Federal Reserve System, and adding capital gains realized by corporations.

Book and taxable profits follow a very similar pattern over the projection period, growing at average annual rates of 3.7 percent and 3.8 percent, respectively. Differences occur in some years, but they are minor. CBO projects that through 2002, profits will remain relatively stable in dollar magnitude and therefore decline as a share of GDP. In 2003, profits are projected to start growing noticeably, although more slowly than GDP through 2007. Beyond 2007, profits will remain a relatively stable share of GDP.

Table 3-7.
CBO's Projections of Corporate Income Tax Receipts and the Tax Base (By fiscal year)

	Actual 2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Corporate Income Tax Receipts												
In billions of dollars	207	215	217	226	236	246	255	264	276	289	303	319
As a percentage of GDP	2.1	2.1	2.0	2.0	2.0	1.9	1.9	1.9	1.9	1.9	1.9	1.9
Annual growth rate	12.2	3.8	0.7	4.3	4.5	4.2	3.6	3.6	4.4	4.6	5.1	5.1
Corporate Book Profits												
In billions of dollars	920	929	940	965	1,007	1,043	1,081	1,119	1,174	1,231	1,296	1,369
As a percentage of GDP	9.4	9.0	8.6	8.4	8.4	8.2	8.1	8.0	8.0	8.0	8.0	8.1
Annual growth rate	16.3	1.0	1.2	2.7	4.4	3.6	3.7	3.5	4.9	4.9	5.3	5.6
Taxable Corporate Profits												
In billions of dollars	741	753	769	791	826	855	886	915	959	1,004	1,056	1,115
As a percentage of GDP	7.5	7.3	7.1	6.9	6.9	6.8	6.7	6.6	6.6	6.5	6.6	6.6
Annual growth rate	13.8	1.6	2.1	2.9	4.4	3.5	3.6	3.4	4.8	4.7	5.2	5.5
Corporate Receipts as a Percentage of Taxable Profits	28.0	28.6	28.2	28.6	28.6	28.8	28.8	28.9	28.8	28.7	28.7	28.6

SOURCE: Congressional Budget Office.

NOTE: The tax base in this table reflects income as measured by the national income and product accounts rather than as reported on tax returns.

Receipts follow that pattern, so the average tax rate, defined as corporate receipts as a percentage of taxable profits, varies within a relatively narrow band of 28 percent to 29 percent over the projection period.

Social Insurance Taxes

Social insurance taxes follow roughly the same path as wages and salaries (see Table 3-8). The largest components are Social Security (Old-Age, Survivors, and Disability Insurance, or OASDI) taxes and Medicare (Hospital Insurance, or HI) taxes (see Table 3-9). They are calculated as a percentage of covered wages, the former up to a taxable maximum that is indexed to wage growth over time. Consequently, OASDI and HI taxes tend to remain stable as a proportion of income as long as covered wages are a stable share of GDP and the distribution of income from wages remains relatively stable. That relative stability is reflected in CBO's projection of social insurance tax receipts, which are expected to remain nearly flat at 6.6 percent of GDP between 2001 and 2011. As a share of wages and salaries, CBO projects that those receipts will drop by 0.1 percentage point to 13.8 percent in 2001 and then will decline only very slowly thereafter, to 13.7 percent through 2011. Since the July report, CBO's projection of social insurance receipts has increased by about $130 billion over 2001 to 2010. That increase is due almost entirely to CBO's revised economic forecast.

Projected social insurance taxes drop as a fraction of wages in 2001 largely because the Treasury Department adjusted its 2000 tabulation of Social Security receipts to reflect previous misestimates, and CBO expects no similar adjustment in 2001. When OASDI and HI taxes are withheld from paychecks and remitted to the Treasury, they are indistinguishable from the individual income tax withholding that is remitted at the same time. The social insurance portions of the payments are estimated and assigned to the respective trust funds on the basis of Treasury's projections. As an accounting of the payments becomes available in the following years, the trust funds are adjusted to make up for any shortfall or excess in the estimates. As a result, lump-sum adjustments of social insurance tax receipts (with offsetting adjustments in individual income tax receipts) may occur in years other than those in which the payments were received and the liabilities in-

Table 3-8.
CBO's Projections of Social Insurance Tax Receipts and Tax Base (By fiscal year)

	Actual 2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Social Insurance Tax Receipts												
In billions of dollars	653	686	725	762	797	840	879	921	963	1,010	1,059	1,110
As a percentage of GDP	6.6	6.6	6.7	6.6	6.6	6.6	6.6	6.6	6.6	6.6	6.6	6.6
Annual growth rate	6.7	5.1	5.7	5.1	4.6	5.4	4.7	4.7	4.6	4.9	4.8	4.8
Wages and Salaries												
In billions of dollars	4,696	4,965	5,246	5,535	5,813	6,097	6,392	6,702	7,027	7,368	7,733	8,118
As a percentage of GDP	47.8	48.1	48.2	48.2	48.2	48.2	48.1	48.1	48.1	48.0	48.0	48.0
Annual growth rate	6.7	5.7	5.7	5.5	5.0	4.9	4.8	4.8	4.9	4.8	5.0	5.0
Social Insurance Receipts as a Percentage of Wages and Salaries	13.9	13.8	13.8	13.8	13.7	13.8	13.8	13.7	13.7	13.7	13.7	13.7

SOURCE: Congressional Budget Office.

NOTE: The tax base in this table reflects income as measured by the national income and product accounts rather than as reported on tax returns.

curred. In 2000, such an adjustment increased social insurance receipts by about $3 billion (an increase in OASDI taxes of $4 billion and a reduction in HI taxes of $1 billion). By their nature, these adjustments are unpredictable. Consequently, CBO makes no comparable or offsetting adjustments for 2001 or any other year in the projection period. Hence, social insurance taxes fall slightly as a percentage of wages in 2001 and are unaffected thereafter.

The very slow decline in social insurance receipts as a fraction of wages and salaries after 2001 is driven largely by revenues associated with Social Security and federal retirement programs. Revenues from Social Security retirement programs as a share of wages will fall slightly over the projection period as the portion of wages subject to Social Security taxes continues to decline gradually. Revenues from federal retirement programs—most of the "other retirement" category —will also decline slightly as federal workers under the old Civil Service Retirement System (CSRS), which has higher contribution rates, retire.

The projected level of receipts from the unemployment insurance program (including both the state and federal components of the unemployment tax system) fluctuates somewhat between 2001 and 2011. The recent extended period of high employment has caused benefit outlays to decline generally in recent years and thereby has permitted states to lower their contributions. For this reason, receipts in 2001 are projected to decline slightly. In 2003, according to CBO's projection, the Federal Unemployment Tax Act trust fund will reach its statutory cap, causing the federal government to transfer additional revenues to the states, permitting the states to further lower their unemployment tax rates and causing unemployment insurance receipts to decline the next year. Beyond 2004, however, unemployment insurance receipts will gradually increase, at a rate slightly faster than the increase in wages. CBO projects the unemployment rate to gradually increase through 2009, which causes benefit outlays, and the receipts that finance those outlays, to increase faster than wages.

Excise Taxes and Other Sources of Revenue

Excise taxes are expected to continue their long-term decline as a percentage of GDP, falling from their share of 0.7 percent in fiscal year 2000 to 0.6 percent toward the end of the projection period. Most excise

Table 3-9.
CBO's Projections of Social Insurance Tax Receipts, by Category (By fiscal year, in billions of dollars)

	Actual 2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Social Security	481	504	532	561	589	620	649	680	712	746	782	819
Medicare	136	146	155	163	171	180	189	198	208	218	229	240
Unemployment Insurance	28	27	29	30	29	31	32	34	34	37	40	43
Railroad Retirement	4	4	5	5	5	5	5	5	5	5	5	5
Other Retirement	5	4	4	4	4	4	4	4	4	4	3	3
Total	653	686	725	762	797	840	879	921	963	1,010	1,059	1,110

SOURCE: Congressional Budget Office.

taxes—those representing about 80 percent of total excise tax receipts—are levied per unit of good or per transaction, rather than as a percentage of value. Thus, although excise receipts grow with real output, they do not rise with inflation and therefore do not grow as fast as nominal GDP. CBO's current projection of excise taxes is changed little from that of July.

Nearly all excise taxes fall into five major categories: highway, airport, telephone, alcohol, and tobacco taxes. Almost half of all excise tax receipts are for the Highway Trust Fund, primarily from gasoline and diesel taxes (see Table 3-10). Most airport and telephone taxes are levied on a percentage basis, so they grow faster than other excise taxes. A small hike in tobacco taxes enacted in 1997 will increase the level of receipts in 2002. However, the projection of tobacco tax receipts also reflects the drop in tobacco consumption that is expected to result from the higher tobacco prices caused by the industry's settlements with the states. The net effect, CBO believes, is that tobacco receipts will be stable after 2003.

Smaller amounts of revenue come from estate and gift taxes, customs duties, and numerous miscellaneous sources (see Table 3-11). Estate and gift tax receipts have tended to grow more rapidly than income because the unified credit for the estate and gift tax, which effectively exempts some assets from the tax, is not indexed for inflation. (The annual exclusion for gifts is indexed for inflation, but the $10,000 maximum annual exclusion will not change until the cumulative inflation since 1997 is at least 10 percent.) By 2006, however, a higher unified credit enacted in the Taxpayer Relief Act of 1997 will be phased in, more than offsetting the absence of indexing and tending to reduce receipts relative to GDP. At the same time, however, the aging of the population will tend to increase estate tax receipts. These effects combine to cause estate and gift taxes as a share of GDP to decline slightly until 2006 and then slowly rise again through the end of the projection period.

Customs duties grow over time in tandem with imports. Their growth will be restrained in the next few years, however, as tariff reductions enacted in 1994 are phased in.

The largest component of miscellaneous receipts is the profits of the Federal Reserve System, which are counted as revenues when turned over to the Treasury. Those profits depend on interest rates and the system's gains and losses on its foreign cur-

Table 3-10.
CBO's Projections of Excise Tax Receipts, by Category (By fiscal year, in billions of dollars)

	Actual 2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Highway	35	36	37	38	39	40	41	43	44	45	46	47
Airport	10	10	11	12	13	13	14	15	16	16	17	18
Telephone	6	6	6	7	7	8	8	8	9	9	10	11
Alcohol	8	8	8	8	9	9	9	9	9	9	9	10
Tobacco	7	7	8	8	8	8	8	8	8	8	8	8
All Other	3	3	3	3	3	3	3	3	3	3	3	3
Total	69	71	74	76	78	81	83	86	88	91	94	97

SOURCE: Congressional Budget Office.

Table 3-11.
CBO's Projections of Other Sources of Revenue (By fiscal year, in billions of dollars)

	Actual 2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Estate and Gift	29	30	32	34	35	36	37	39	43	46	48	52
Customs Duties	20	21	23	24	25	26	27	27	28	29	30	31
Miscellaneous												
Federal Reserve	32	24	29	30	32	33	34	36	38	40	42	44
Universal Service Fund	5	5	6	8	13	13	13	13	13	13	13	14
Other	6	6	6	6	6	6	6	5	5	5	5	5
Subtotal	43	36	41	44	51	52	54	55	57	59	61	63
Total	92	87	96	102	111	114	117	121	128	133	139	147

SOURCE: Congressional Budget Office.

rency holdings. An act making consolidated appropriations for fiscal year 2000 (Public Law 106-113), however, required the Federal Reserve to turn over to the Treasury about $3.8 billion of its "surplus," or capital (the cumulation of earnings that the Federal Reserve previously retained), which raised the contribution of Federal Reserve receipts to the Treasury for that year. But the Federal Reserve is rebuilding its capital in 2001 by reducing the amount of receipts that it would otherwise turn over. Consequently, those receipts are expected to be lower in 2001 and then to resume their normal level.

Another significant component of miscellaneous receipts is the Universal Service Fund. Collected from telecommunications companies, money from the fund is intended to finance Internet service for libraries and schools in low-income areas and subsidize basic telephone service for high-cost areas and low-income households. That source of revenue hovers close to $5 billion until 2003, then more than doubles as more elements of the program get under way.

The Stock Market and CBO's Revenue Projections

CBO's estimates of revenues remain above 20 percent of GDP throughout the projection period. At the end of the period, in 2011, the share is projected to be 20.4 percent, not very much less than the share in 2000, and much higher than the postwar norm. The surge in revenues in the late 1990s was fueled by phenomena that are only imperfectly understood. The extraordinary rise in the stock market has been repeatedly cited as a potential explanation. So the question arises of whether CBO's revenue projections depend on a continuation of the stock market boom of the late 1990s.

There are many possible means by which the stock market can affect receipts. Two have received special attention from analysts: capital gains realizations and income from stock options. The rising prices of financial assets increase the accrual of capital gains, which ultimately lead to taxable realizations. Income from stock options exercised in any given year typically represents the appreciation of the stock price from the time the option was issued to the time it is exercised, so that income from options too —and the tax receipts thereby generated—is swelled by a rising market.

CBO does not build a forecast of stock prices into its projections. Its projections of capital gains are based largely on the historical relationship between realizations and the size of the overall economy. As a result, the current projections assume that receipts from capital gains will decline from their current high levels to levels more consistent with

their historical relationship to the size of the economy. CBO does not include stock options separately in its models but rather as part of the projection of wage and salary income. The offsetting effect of option income on individual and corporate receipts, however, indicates that whatever their size, their impact on overall receipts is likely to be small. The main reasons that the receipts-to-GDP ratio remains high over the projection period are the progressive structure of the income tax and the AMT.

Capital Gains Realizations

Capital gains can generate receipts in a variety of ways. They affect the taxable bases of both the individual income tax and the corporate income tax. Moreover, they affect individual income receipts through different routes. Most significantly, they appear as income on 1040 forms. But they also affect the income of trusts and estates, which is taxed under the individual income tax. They also affect receipts in other less significant ways not discussed here.

Table 3-6 shows actual and projected capital gains receipts from individuals. As shown in Table 3-3, capital gains realizations have been a major reason for the increase in individual income tax liabilities relative to GDP. As a proportion of individual income tax receipts, they have grown from about 6 percent or 7 percent at the beginning of the 1990s to nearly 12 percent. The contribution of corporate capital gains to receipts is considerably smaller. Although data are not available to separately identify the income tax receipts from estates and trusts that are due to capital gains realizations, much of the recent growth of those receipts is probably due to increased realizations of gains. Under an extreme assumption that would count all of the receipts from estates and trusts as from gains realizations, total receipts from those three sources of capital gains taxation were possibly as high as 5 percent of all revenues in fiscal year 1995 and 9 percent in fiscal year 2000.

The methods used for projecting receipts from capital gains realizations over the long term are consistent with a number of different scenarios for the stock market. A significant amount of realizations comes from assets other than stocks, especially real estate. Moreover, movements in realizations are not contemporaneous with movements in asset prices. Accrued gains are not taxed until taxpayers realize the gains when they sell the assets. At any given time, a great many accrued gains are available for realization and taxation, depending on taxpayers' decisions about when to sell their assets. Consequently, realizations (and the taxable income they generate) may lag well behind a market increase. And high stock market volume, even in the face of falling stock prices, may generate substantial taxable gains as earlier appreciation of assets is finally realized.

CBO's projections of receipts from individual income taxes and corporate income taxes do not depend on a continuation of the stock market surge, or even growth at the historical average rate—which is most clearly evident in the projections of liabilities from capital gains realizations under the individual income tax. Those gains reported on 1040 forms are an important reason why the ratio of receipts to GDP is projected to fall over the next few years. Specifically, gains for tax year 2000 are expected to rise on the basis of the behavior of the market and the economy in that year; and those receipts will partly show up in fiscal year 2001 revenues. But receipts from gains are then projected to fall as a percentage of taxes and of GDP after fiscal year 2001, throughout the projection period, so by the final three years, gains will account for roughly the same percentage of individual income tax receipts that they did in the early 1990s.

Stock Options

Employee stock options usually generate income tax receipts when they are exercised. Tax rules require that income earned on most stock options be reported as wage and salary income. Neither the tax data nor the NIPAs break out option income from other wage and salary income. Estimates derived from corporate financial reports suggest that option income was on the order of 1 percent to 2 percent of wage and salary income in calendar year 1999, or about $50 billion to $100 billion. With much of it probably concentrated among taxpayers paying the higher marginal rates, the result would have been roughly $15 billion to $30 billion of individual income tax receipts.

Nonetheless, a significant amount of option income would still be generated in a less robust market. Even in a generally falling market, some prices still rise. In addition, if the market failed to supply option income for employees, firms would likely replace at least some with other forms of compensation. Consequently, the drop in individual income tax receipts that would come from the effect of a sluggish stock market on option income would presumably be less than the total amount of receipts from such income.

Most important, because income from realized options is deductible for purposes of the corporate income tax, the impact on total receipts is less than that implied by a reduction in the option income of individuals. Every dollar of option income realized by individuals generates a dollar reduction in corporate profits. The positive net revenue impact of option income in the year of realization, therefore, is largely limited to options realized by employees of unprofitable firms, which pay no income tax anyway and for which the additional deduction has no effect on their tax liability.[3] Consequently, given the largely offsetting effects on corporate receipts, even a substantial fall in option income would probably generate only a small decline in total taxable income, so the bottom-line impact on total receipts would likely be minor.

In short, CBO's revenue projections are not based on implicitly optimistic or pessimistic assumptions about the stock market's performance. The factors known to have driven the recent surge in revenues are not assumed to continue as they have over the past few years. But they are not assumed to go away completely either and are projected to continue contributing to revenues over the projection period. The projection has both upside and downside risks. The receipts-to-GDP ratio remains high over the period primarily because of the progressive structure of the income tax and the AMT. It is not an assumption of a continuing strong stock market that drives the revenue projections, but the effect of growing incomes on the effective tax rate.

3. There may still be an offsetting deduction in a future year should the corporation become profitable for tax purposes.

Expiring Tax Provisions

CBO's revenue projections assume that current tax law remains unchanged and that scheduled changes and expirations occur on time. The sole exception to that approach is CBO's treatment of the expiration of excise taxes dedicated to trust funds. Under the rules governing the construction of CBO's projections, those taxes are included in the revenue projections even if they are scheduled to expire.

The largest trust fund excise taxes that are slated to expire during the next decade finance the Highway Trust Fund. Some of the taxes for that fund are permanent, but most of them expire on September 30, 2005. Extending those taxes at today's rates contributes about $39 billion to CBO's revenue projection in 2011, about 40 percent of total excise tax receipts.

The assumed extension of other expiring trust fund taxes accounts for smaller amounts in 2011. Taxes dedicated to the Airport and Airway Trust Fund, scheduled to expire at the end of fiscal year 2007, contribute about $17 billion in revenues in 2011. Taxes for the Leaking Underground Storage Tank Trust Fund, set to expire on March 31, 2005, contribute about $250 million in 2011. No other expiring tax provisions are automatically extended in CBO's projections.

Twelve provisions are slated to expire by the end of 2001 (see Table 3-12). Because they provide tax benefits, they would all reduce revenues if extended. Extending all of them through at least 2011 would lower revenues by a total of about $81 billion over the projection period and by $16 billion in 2011. Over the period, about $42 billion of that cost, or about half, would come from the provision that allows individuals to claim certain personal credits against the AMT. Without that provision, as assumed in CBO's projections beyond 2001, some taxpayers would be unable to claim the child and education tax credits that were enacted in the Taxpayer Relief Act of 1997. The provision allowing an exemption from taxable income for certain financing income earned abroad would reduce revenues by an estimated $21 billion if extended at least through 2011. Extending the Generalized System of Prefer-

Table 3-12.
Effect of Extending Tax Provisions That Will Expire Before 2011 (By fiscal year, in billions of dollars)

Tax Provision	Expiration Date	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Total, 2001-2011
Provisions Expiring in 2001													
Generalized System of Preferences	9/30/01	n.a.	-0.5	-0.5	-0.5	-0.6	-0.6	-0.6	-0.7	-0.7	-0.7	-0.8	-6.3
Andean Trade Preference Initiative	12/4/01	n.a.	*	*	*	*	*	*	*	*	*	*	-0.3
Credits for Electricity Production from Wind and Biomass	12/31/01	n.a.	*	*	*	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.7
Deductions for Clean-Fuel Vehicles and Refueling Property	12/31/01	n.a.	*	*	*	*	*	*	*	*	*	*	-0.3
Exclusion for Employer-Provided Education Assistance	12/31/01	n.a.	-0.4	-0.4	-0.4	-0.4	-0.4	-0.5	-0.5	-0.5	-0.6	-0.6	-4.6
Net Income Limitation for Marginal Properties	12/31/01	n.a.	*	*	*	*	*	*	*	*	*	*	-0.4
Qualified Zone Academy Bonds	12/31/01	n.a.	*	*	*	*	*	*	-0.1	-0.1	-0.1	-0.1	-0.4
Subpart F for Active Financing Income	12/31/01	n.a.	-0.3	-1.3	-1.4	-1.7	-1.9	-2.2	-2.5	-2.9	-3.3	-3.8	-21.2
Credit for Electric Vehicles	12/31/01	n.a.	*	*	*	*	*	*	-0.1	-0.1	-0.1	-0.1	-0.4
Treatment of Nonrefundable Personal Credits Under the AMT	12/31/01	n.a.	-0.3	-1.4	-1.7	-2.4	-3.2	-4.1	-5.3	-6.4	-7.9	-9.7	-42.2
Welfare-to-Work Credit	12/31/01	n.a.	*	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-1.2
Work Opportunity Credit	12/31/01	n.a.	-0.1	-0.2	-0.3	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4	-3.6

(Continued)

ences, which provides nonreciprocal tariff preferences to many developing countries, would reduce revenues by about $6 billion. If extended, the provisions that allow an exclusion for certain employer-provided educational assistance and provide a work opportunity tax credit would reduce revenues by $4.6 billion and $3.6 billion, respectively.

Twelve provisions expire between 2002 and 2011, seven of which would reduce revenues if extended. The one with the largest revenue effect by far is the research and experimentation tax credit, which was first enacted in 1981 and affects businesses. In 1999, the Congress extended that tax benefit for the ninth time since 1985. That extension (through June 2004) is its longest. Extending that provision through 2011 would reduce revenues by about $29 billion through 2011. The other five revenue-losing provisions expiring after 2001 were all recently extended in the Community Renewal Tax Relief Act of 2000. Combined, they would reduce revenues by about $6 billion through 2011 if extended.

Four provisions that expire between 2002 and 2011 would raise revenues if extended. Extending the luxury tax on passenger vehicles and the abandoned mine reclamation fees would each raise revenues by about $2 billion. Extending the Internal Revenue Service's user fees and the provision that allows

Table 3-12.
Continued

Tax Provision	Expiration Date	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Total, 2001-2011
Provisions Expiring Between 2002 and 2011													
Medical Savings Accounts	12/31/02	n.a.	n.a.	*	*	*	*	*	*	*	*	*	-0.1
Luxury Tax on Passenger Vehicles	12/31/02	n.a.	n.a.	0.2	0.2	0.2	0.2	0.3	0.3	0.3	0.3	0.3	2.2
IRS User Fees	9/30/03	n.a.	n.a.	n.a.	**	**	**	**	**	**	**	**	0.3
Corporate Contributions of Computers to Schools	12/31/03	n.a.	n.a.	n.a.	-0.1	-0.1	-0.1	-0.1	-0.2	-0.2	-0.2	-0.2	-1.2
Brownfields Environmental Remediation	12/31/03	n.a.	n.a.	n.a.	*	-0.1	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-1.5
District of Columbia First-Time Homebuyer Credit	12/31/03	n.a.	n.a.	n.a.	*	*	*	*	*	*	*	*	-0.2
Tax Incentive for Investment in the District of Columbia	12/31/03	n.a.	n.a.	n.a.	*	-0.1	-0.1	-0.1	-0.1	-0.2	-0.2	-0.2	-1.0
Credit for Research and Experimentation	6/30/04	n.a.	n.a.	n.a.	-0.4	-2.5	-3.2	-3.8	-4.3	-4.7	-4.9	-5.0	-28.8
Abandoned Mine Reclamation Fees	9/30/04	n.a.	n.a.	n.a.	n.a.	0.2	0.2	0.2	0.2	0.2	0.2	0.2	1.7
Transfer of Excess Assets in Defined Benefit Plans	12/31/05	n.a.	n.a.	n.a.	n.a.	n.a.	**	**	**	**	**	**	0.2
FUTA Surtax of 0.2 Percentage Points	12/31/07	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	0	0	0	0	0
Empowerment Zones	12/31/09	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	-0.6	-1.2	-1.7
All Expiring Provisions													
Total		n.a.	-1.6	-3.8	-5.0	-8.1	-10.0	-12.0	-14.1	-16.1	-19.0	-22.0	-111.6

SOURCES: Joint Committee on Taxation, Congressional Budget Office.

NOTES: n.a. = not applicable; AMT = alternative minimum tax; IRS = Internal Revenue Service; FUTA = Federal Unemployment Tax Act.

* = loss of less than $50 million.

** = gain of less than $50 million.

employers to transfer excess assets in defined benefit plans to a special account of health benefits for retirees would each raise less than $50 million a year.

One provision has no effect on revenues. Although the Federal Unemployment Tax Act surcharge brings in about $2 billion a year, the additional income would be passed to the states. CBO assumes that the states would then use those rebates to lower their unemployment insurance tax rates. Since the state taxes are also part of federal unemployment tax receipts, extending the surcharge would have no net effect on revenues.

If all expiring provisions were extended, CBO's projections of revenues would be lower by $22 billion in 2011 and by $112 billion over the projection period.